

**INITIAL STATEMENT OF REASONS
FOR THE ADOPTION OF RULES UNDER THE
REAL ESTATE APPRAISERS' LICENSING AND CERTIFICATION LAW**

As required by Section 11346.2(b) of the Government Code, the Director of the Office of Real Estate Appraisers ("OREA") sets forth below an initial statement of reasons for the proposed amendments to California Code of Regulations, Title 10, Chapter 6.5 of Sections 3500, 3522, 3523, 3524, 3526, 3527, 3528, 3529, 3530, 3575, 3576, 3577, 3582, 3681, 3702, 3703, 3721, 3724, 3726, 3728, 3731, and 3741.

The Real Estate Appraisers' Licensing and Certification Law (Business and Professions Code, Division 4, Part 3, Section 11313) requires the Director of OREA to adopt and enforce rules and regulations as are determined reasonable necessary to carry out its purposes. The Director proposes amendments to regulations adopted under that authority to implement amendments to the Real Estate Appraisers; Licensing and Certification Law from Senate Bill 237 (Statutes of 2009, Chapter 173) ("SB 237"). SB 237 authorizes the Director of OREA to register appraisal management companies as defined under Section 11302(d) of the Business and Professions Code ("Code"). All Code section references are to the Business and Professions Code unless otherwise specified.

1. Section 3500. Meaning of Words and General Definitions

Problem

Existing regulations include general definitions for key words or phrases employed to regulate the licensing and certification of appraisers within the state of California. The passage of SB 237 gives OREA authority to regulate appraisal management companies through a registration process. Because of this new regulatory authority, a series of additional definitions are required.

Specific Purpose and Necessity

The statute provides definitions for the following: Appraisal Management Company, Certificate of Registration, Controlling Person, and Registration. The relevant terms under Section 3500 mirror these statutory definitions. In addition, the Director of OREA proposes new terms: "Designated Officer" and "Registrant" to further identify and clarify the implementation process of appraisal management company registration.

2. Section 3522. License or Certificate of Registration

Problem

Section 11320.5 of the statute enacted by SB 237 states that: "No person or entity shall act in the capacity of an appraisal management company without first obtaining a certificate of registration from the office." This section of the statute provides the underlying authority for OREA to issue certificates of registration to appraisal management companies.

Specific Purpose and Necessity

This section of existing regulation sets forth the requirements for the necessary content of the information to be included on the face of an appraiser's license. This section is further supplemented with the requirements for information to be included with the certificates of registration for appraisal management companies. The registration contains information important to the public including the name of the registrant, the registration number, any registration restrictions, and the date of issuance and expiration of the registration.

3. Sections 3523, 3524, 3526, 3527, 3529, 3530

Problem

The above-referenced sections of the regulations define standard operating terms and procedures for licensed appraisers. These sections govern the term of the license, consent to service of process, changes to personal or contact information, and restrictions on the licensing for aliens. In addition, licensees are notified that licenses are considered the property of OREA and that licensee records are subject to audit by OREA. These existing sections of the regulations do not apply to holders of certificates of registration.

Specific Purpose and Necessity

It is necessary to supplement these sections in order to make the standard operating terms and procedures applicable to holders of certificates of registration for appraisal management companies.

There is a change in the Emergency Regulations filed January 21, 2010 in Section 3527 to include a new form REA 5011 (Appraisal Management Company Change Notification and Miscellaneous Requests), as the Change Notification form for appraisers was not adaptable to appraisal management companies.

4. Section 3528. Minimum Requirements

Problem

This section addresses the minimal requirements for appraisers in order to receive a license from OREA. This section must also reference the minimum qualification requirements for holders of certificates of registration as appraisal management companies.

Specific Purpose and Necessity

The minimum requirements for certificates of registration for appraisal management companies must be referenced within this section. In Article 4 of the regulations, Sections 3575 and 3576, the specific requirements for certification are set forth (detailed below). This section is merely a reference to Sections 3575 and 3576. In the Emergency Regulations filed January 21, 2010, Sections 3528(d) and (e) provided for the issuance of conditional certificates of registration. The certificate of registration requirement became effective on the statutory effective date of January

1, 2010, the same day that OREA became authorized to promulgate regulations. It was necessary to issue conditional certificates of registration during the Emergency Regulation period to enable applicants to temporarily continue operation in California while OREA conducted the regular rulemaking procedure. The conditional certificates of registration could not exceed 150 days from the date of issuance, during which time OREA would complete the statutorily required application review. There is no longer a need to issue conditional certificates of registration; therefore, Sections 3528(d) and (e) are deleted from the regular rulemaking regulations text.

5. Section 3575. Application

Problem

The existing regulations do not include provisions for the application process for the registration of appraisal management companies. New Business and Professions Code Sections 11345 and 11345.05 grant authority to the Director of OREA to adopt regulations governing the process and procedures of applying for registration as an appraisal management company. The Director of OREA proposes adding Section 3575 to delineate the requirements for the application process for appraisal management companies.

Specific Purpose and Necessity

Section 3575 establishes key elements in the application process for appraisal management companies. Subsections 3575(a) and 3575(b) add registration parameters regarding the term of the application and requirements for knowledge of the English language and arithmetic computations common to real estate appraisers that are consistent with appraisal licensing applications in Section 3561. Subsections 3575(c), (d), and (e) specify the forms to be used for the application process. These forms include applications for both the Certificate of Registration for the appraisal management company (REA 5001) and for the controlling persons (REA 5002).

The Director of OREA proposes changes to forms REA 5001 and REA 5002 as incorporated into the Emergency Regulations to reflect the addition of specific service of process provisions to the certification by the Designated Officer and removal of these provisions from the Agent for Service of Process certification. This change is necessary to identify the Designated Officer, rather than the Agent for Service of Process, as the appropriate party to consent to service of process provisions on behalf of the appraisal management company.

6. Section 3576. Background requirements for Controlling Persons in Appraisal Management Companies

Problem

It is important that a Controlling Person for an appraisal management company meets certain background requirements involving trustworthiness. Appraisal management companies represent a business that involves a trust relationship with their clients; the lenders. SB 237 added Business and Professions Code Section 11345.2 to restrict individuals with a history of specified licensing or criminal infractions from acting as Controlling Persons in a registered

appraisal management company. The Director of OREA proposes new Section 3576 to address these background requirements.

Specific Purpose and Necessity

The Director of OREA proposes new subsections 3576 (a), (b), and (c) to reiterate and clarify the restrictions in Business and Professions Code Section 11345.2. These subsections prohibit any individual from acting as a Controlling Person for a registered appraisal management company if that person has been convicted or pled guilty or no contest to a felony or have had an appraisal license, certification, or real estate license denied, cancelled, or revoked in California or any other state. Subsection (c) also specifies that a registered controlling person must notify OREA of the occurrence of any of these events within ten days of their knowledge of the fact. Subsection (d) provides that applicants for controlling persons must submit to OREA the appropriate certifications that they are licensees in good standing in any other jurisdiction in which they may hold an appraisal license. Subsection (e) specifies that applicants for controlling persons must submit fingerprints to the Department of Justice to be used for obtaining information relating to records of arrests and convictions. This is consistent with the requirements for licensed real estate appraisers. It is important that each appraisal management company have a primary contact for dealing with OREA. This individual is the Designated Officer and would be the focal point for dialogue regarding questions or complaints involving the appraisal management company. The requirement that this individual be identified is in subsection 3576(f).

7. Section 3577. Minimum Standards of Practice for Appraisal Management Companies

Problem

Appraisal Management Companies must adhere to minimum standards of practice when acting as an intermediary between their lending clients and the appraisers they contract with. It is imperative that the appraisal management companies act in an ethical manner. Business and Professions Code Sections 11345.3, 11345.4, 11345.45, and 11345.6 establish the minimum standards of practice for appraisal management companies. This is the basis for codification into the regulations. They are further delineated in the regulations to ensure protection of the appraisers as they operate in conformance with the Uniform Standards of Professional Appraisal Practice. These standards are published by the Appraisal Standards Board of the Appraisal Foundation. Section 3701 of the existing regulations requires that licensed and certified appraisers within California conform to and observe the Uniform Standards of Professional Practice as promulgated by the Appraisal Foundation.

Specific Purpose and Necessity

This section is instrumental in establishing the fundamental business practices that appraisal management companies must adhere to. Section 3577 restates in concept the required business practices set forth in Business and Professions Code Sections 11345.3, 11345.4, and 11345.6. It is further augmented and clarified to reflect ethical obligations imposed on appraisers through the Conduct Section of the Ethics Rule of the Uniform Standards of Professional Practice. It is

important that appraisal management companies understand and support the ethical obligations that licensed and certified appraisers are mandated to comply with.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (HR 4173), signed into law on July 21, 2010, contains an amendment to the Real Estate Settlement Procedures Act of 1974 that provides for a clear disclosure of the amount paid to appraisers, as differentiated from the “administration fee” charged by appraisal management companies. Accordingly, Subsection (d) of Section 3577 requires that appraisal management companies maintain records of all fees dispersed to appraisers. Under subsection (e), an appraisal management company cannot prohibit an appraiser from disclosing the fee paid to the appraiser within the body of the appraisal report. The inclusion of these clauses will assist in preventing unnecessary and exorbitant charges, increase consumer protection, and support the intent of the new federal statute.

Appraisal management companies cannot exert undo influence on real estate appraisers as stated in subsection (f) (1) of Section 3577. It is important to clarify, however, that appraisers are responsible for effectively communicating assignment results and providing additional information subsequent to the assignment completion, if required to enhance the credibility of the appraisal report. Section 3577 subsections (f) (2) (A), (B), and (C) allow appraisal management companies to request additional information if the appraisal is deficient in its analysis.

There are several significant changes to Section 3577 of the Emergency Regulations. In Section 3577(b), appraisal management companies were required to ensure that all appraisal assignments were performed in accordance with the Uniform Standards of Professional Appraisal Practice. There was considerable public comment regarding this requirement. In response to these comments, the proposed Section 3577(b) now requires that appraisal management companies have reasonable procedures in place that are designed to ensure that all assignments are performed in compliance with the Uniform Standards of Professional Appraisal Practice. This would include auditing procedures or reviews of specific assignments. Subsections (a) and (b) needed to clarify that both independent contractor and employee appraisers must possess the appropriate licenses and that they must comply with the Uniform Standards of Professional Appraisal Practice. Section 3577(f)(1) added the language “...or attempt to improperly influence...” pursuant to Business and Professions Code Section 11345.4 of the statute. In response to a public comment made regarding Section 2577(f)(1)(A), additional language clarifies and emphasizes the objective of promoting compliance with the Uniform Standards of Professional Appraisal Practice. Whether or not a completed assignment meets relevant standards was not considered in the Emergency Regulations language of this subsection. Section 3577(g) of the Emergency Regulations is deleted in the regular rulemaking submission, as it is beyond the scope of the underlying statute.

8. Section 3582. Fee Schedule

Problem

The existing fee structure was developed to cover OREA's costs for licensing and enforcement of state law governing real estate appraisers. SB 237 requires OREA to establish and implement an entirely new program to register and regulate appraisal management companies as entities distinct from individual real estate appraisers. Existing fees will not cover the costs of developing and implementing this new program and individual appraisers should not bear the cost of regulating appraisal management companies through the payment of licensing fees.

OREA staff estimates that there will be approximately 150 registrants and 200 complaints in the first full year of appraisal management company registration. This would mandate an enforcement workload of .84 personnel years for a Property Appraiser Investigator position (1,504 hours – annual salary with overhead: \$118,996) and .12 personnel years for a Legal Counsel position (216 hours – annual salary with overhead: \$159,999), resulting in total enforcement costs of approximately \$120,000. An annual registration fee of \$800 for 150 appraisal management companies will cover the costs of the registration and enforcement program. This amount is at the lower end of the registration fees that are being charged by other states throughout the nation that have implemented appraisal management company legislation.

Specific Purpose and Necessity

The Director proposes a \$150 application review fee to cover the cost of evaluating an applicant's eligibility to receive a certificate of registration as an appraisal management company. This review includes evaluating the individual application from each Controlling Person as identified by the registration applicant. The Director also proposes a fee of \$1,600 for issuance of a new or renewed certificate of registration, with renewal of certification required every two years. The new fees proposed in Section 3582 for review and approval of an appraisal management company's application for registration are based on the projected workload for registration and enforcement of an estimated number of appraisal management company applicants in any one year.

An additional change to the Fee Schedule from the Emergency Regulations filed January 21, 2010 is to change Section 3582(b)(7) from the current Federal Registry Fee of \$50 (\$25 per year) for appraisers to "as prescribed by the ASC." HR 4173, referenced in #7 above, also provides for an increase in National Registry fees for appraisers and for the collection of National Registry fees for appraisal management companies. The timing of implementation for the appraisal management company registry fee and for future fee amount changes is the responsibility of the ASC, and is unknown at this time.

9. Section 3681. Renewal Applications

Problem

SB 237 provides the Director with criteria to review and approve initial applications for certificates of registration, but does not address registration renewal other than identifying two

years as the standard certificate period, subject to extension or limitations imposed within the Director's discretion. State law regards an appraiser's license as a property right to which licensees are presumed entitled, subject to minimal requirements including the absence of disciplinary actions substantially related to the licensees' appraisal practice. In addition, applicants for license renewal must demonstrate compliance with continuing education requirements and timely submittal of the renewal application accompanied by payment of the appropriate fee. The existing language in Section 3681 reflects these minimal requirements for renewal of an appraisal license.

Specific Purpose and Necessity

The Director proposes new language in Section 3681 to impose application requirements for registration renewal that are comparable to the existing requirements for appraisal license renewal. The proposed language changes the education requirements imposed by subsection 3681(d) (2) of the Emergency Regulations, which require each Controlling Person to complete seven hours of USPAP-related continuing education, including nonappraisers functioning as Controlling Persons. Based on comments received on this provision, the Director proposes new language which limits this 7-hour continuing education requirement to one designated Controlling Person who is involved in the appraiser selection approval process. Additionally, the Emergency Regulations require "...proof of completion of the 7-hour continuing education course, USPAP for non-appraisers." This course has not yet been developed, and it is not known if it will be available when the first appraisal management company renewal period occurs in January 2012. Therefore, the text of the Emergency Regulations has been changed to require the existing 7-hour National USPAP Update Course, approved by the Appraiser Qualifications Board of the Appraisal Foundation.

Subsection 3681(d) (3) in the Emergency Regulations provides for a certification from a Designated Officer that the appraisal management company has complied with state statutes and regulations in the previous two-year period when applying for renewal of a certificate of registration. This has been appropriately edited to require the use of the Appraisal Management Company Renewal Application form REA 5012, which contains the certification that has been deleted from this subsection.

10. Section 3702. Special Qualifications of Appraisers and Controlling Persons of Appraisal Management Companies

Problem

Appraisal management companies have a trust relationship with their clients; the lenders for federally-related transactions. As such, appraisal management companies and their associated Controlling Persons have a responsibility to both their clients and the public to generate and maintain a culture based on ethical and competent standard business practices. These practices must be comparable to those required of appraisers under the USPAP because appraisal management companies represent the critical intermediary linking the appraiser's services to the clients' needs. However, USPAP does not apply to appraisal management companies as organizations nor to Controlling Persons who are not licensed appraisers.

Specific Purpose and Necessity

Existing Section 3702 specifies that licensed appraisers demonstrate by their conduct the qualifications of honesty, candor, integrity and trustworthiness substantially related and indispensable to the practice of the appraisal profession. The Director proposes new language in Section 3702 to extend these essential standards of conduct to each Controlling Person as key individuals vested with the responsibility to promote and maintain these standards to the operation of the registered appraisal management company as a whole.

11. Sections 3703, 3721, 3724, 3726, 3728, 3731, and 3741

Problem

The above-referenced sections of the existing regulations define the disciplinary process and sanctions for acts of omission or commission by a licensed appraiser, up to and including the revocation of an appraisal license. These sections do not apply to holders of certificates of registration as an appraisal management company.

Specific Purpose and Necessity

The Director proposes to amend the above-referenced sections to include holders of certificates of registration as subject to the existing disciplinary procedures and sanctions.

ALTERNATIVES CONSIDERED

No reasonable alternatives considered by OREA or that have otherwise been identified and brought to the attention of OREA would be more effective in carrying out the purpose for which the action is proposed or would be as effective and less burdensome to affected private persons, or would lessen any adverse impact on small business.

DETERMINATIONS

The Director of OREA has made an initial determination that the proposed regulatory action does not have a significant adverse economic impact on business.